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IN THE

Supreme Court of the United States

October Term, 1947

No.....

CHARLES E. BUNTING,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT AND BRIEF IN SUPPORT THEREOF

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioner by his counsel hereby prays that a writ of *certiorari* issue to review the judgment of the United States Circuit Court of Appeals for the Sixth Circuit entered in the above cause on November 24, 1947, affirming the decision of the Tax Court of the United States entered September 24, 1946.

Opinions Below.

The "Findings of Facts and Opinion" of the Tax Court of the United States appears at pages 27-40, inclusive, of the record and was not officially reported. The opinion of the Circuit Court of Appeals for the Sixth Circuit appears at pages 127 to 134, inclusive, of the record and is reported in 164 F. (2d) 443.

The opinion is inaccurate in certain respects, as follows:

(1) On page 2, line 9 (R. p. 127, line 34) "160" should read "150."

(2) On page 3, in the third line (R. p. 129, line 2) after "Bunting" there has been omitted the following words:

"and further, Donor's son, Charles E. Bunting,". (R. 102.)

(3) On page 5, lines 9 to 13 (R. p. 131, lines 25 to 29, incl.) the opinion reads as follows:

"The trustee was given discretion with reference to holding the securities delivered to it or thereafter added to it, without accounting for loss except with respect to the shares of stock or other securities of the company or its successor."

By ARTICLE III the trustee is given discretion to hold the securities delivered to it and those thereafter added to the trust without accountability for loss arising therefrom, and except as in the trust elsewhere provided with respect to shares of stock or other securities of the Bunting Company, to change or alter the investment included in the trust. (R. 52.)

(4) The second full paragraph on page 5 (R. p. 132) of the opinion reads as follows:

"By ARTICLE IV it was provided that after the death of petitioner and during his life the net income

should be disposed of in accordance with the written directions of petitioner at any time or from time to time, subject to the exercise of the power conferred upon the petitioner."

Section 2 of said ARTICLE IV provides that after the death of the Donor (Fannie Bunting), and during the life of petitioner, the net income shall be disposed of in accordance with the written directions of petitioner, at any time or from time to time given, subject to the exercise of all other power conferred by the trust upon the petitioner. (R. 57.)

Jurisdiction.

The judgment of the Circuit Court of Appeals was filed November 24, 1947. (R. 126.) The jurisdiction of this court is invoked under Sections 22(a), 161 and 162 of the Internal Revenue Acts of 1936 and 1938.

Questions Presented.

The questions presented are:

1. Is the undistributed income of the trust taxable to the petitioner under Section 22(a) of the Internal Revenue Acts of 1936 and 1938 by virtue of the powers granted by the owner of the trust *res* to the petitioner under the terms of the trust, such powers being the right to amend or revoke the trust indenture or to withdraw any of the trust *res* from the operation of the indenture? or

2. Is the undistributed income of the trust taxable to the trust as income accumulated and held for future distribution under Sections 161 and 162 of the Internal Revenue Acts of 1936 and 1938?

Statutes Involved.

The pertinent provisions of Sections 22(a), 161 and 162 of the Internal Revenue Acts of 1936 and 1938 are set forth in the appendix attached hereto and made a part hereof.

Statement.

On January 2, 1929, Fannie Bunting, the petitioner's mother, created the trust involved in this cause, which is known as Trust No. 50. (R. 48, 49.) The dividends of The Bunting Brass & Bronze Company are the principal source of the income of the trust.

That Company was formed in 1907 by petitioner's father, William Bunting, and two other men who were connected with a somewhat kindred business, with a capital of 100 shares of the par value of $100 per share, of which Bunting owned 50 shares and the other interests 50 shares. William Bunting was the husband of Fannie Bunting. (R. 46, 47; Ex. 6, R. 116.)

In 1909 William Bunting became the sole owner of all of the shares of the Company, and immediately moved the Company's plant, which theretofore had been at Alliance, Ohio, to Toledo, Ohio. Shortly thereafter the capital was increased from 100 shares to 1,000 shares, of the par value of $100 each, and at about the time of the increase, he gave his wife 40 shares and each of his three sons 70 shares, retaining 750 shares. (R. 46, 47; Ex. 6, R. 116.)

William Bunting was the president of the Company from the time of its organization until his death in August, 1916. (R. 47.)

Though he was president of the Company, he took an increasingly less active part in the management of it after the plant was moved to Toledo. (R. 47, 48.) His three sons, William H., John W. and Charles E., the petitioner,

joined the Company shortly after its inception. (R. 47.) The oldest brother was born in 1872, John in 1882, and Charles in 1886. (R. 46.) The oldest brother was the superintendent, the second one was the salesman, and Charles was the manager, under the direction of the father. (R. 47.)

Under the terms of William Bunting's will, which was executed in January of 1916, he bequeathed all of the 750 shares of the Company which he owned at that time to his wife and sons, 150 shares to each of his sons, William and John, 225 shares to his wife and 225 shares to petitioner, subject to the stipulation that all of said 750 shares were to be held by his wife and son, Charles, as joint trustees for the legatees for a period of fifteen years from the date of testator's death, unless by the mutual consent of all of the legatees the trust was to continue for a further period of time. (Ex. 7, R. 118-121.)

He further directed that the shares should be so retained, unless in the judgment of the Trustees the best interests of the estate demanded that the shares should be transferred at an earlier date to the four legatees. (Ex. 7, R. 119.)

Shortly after the probate of the will the two older sons protested against the provision of the father's will which placed the shares in trust and in effect vested control of their shares in the petitioner. (R. 47.)

In the interest of harmony in the family relationship the Trustees terminated the trust and distributed the shares among the four legatees, as the Trustees were authorized to do under the terms of the will if, in their judgment, it was in the best interests of the trust estate so to do. (R. 47; Ex. 7, R. 119.)

After the distribution of the shares, Fannie Bunting, in order to carry out the expressed wish of her husband that the shares be held intact to preserve unity and control

in the management of the Company, transferred all but one of her shares of the Company to petitioner as trustee, granting him the sole power to vote said shares. (R. 47, 48; Ex. 6, R. 117.)

Prior to 1924, Fannie Bunting had frequently expressed to petitioner her desire to perpetuate the Company and to insure good management for the Company, thereby effecting the evident purposes her husband sought to achieve when he placed the shares of the Company in a trust to continue for a period of fifteen (15) years after his death. (R. 48.)

Finally, on January 18, 1924, Fannie Bunting created an irrevocable trust in which The Toledo Trust Company was designated as trustee and to which she transferred all of the shares of the Company which she then owned. (Ex. 2, R. 94.) By the 1924 trust, the trustee was given broad powers of management of the trust property, subject to the petitioner's right to withdraw all or any of the corpus of the trust. The indenture directed that during the petitioner's lifetime, the trustee should give to petitioner authority to vote the shares of the Company and provided that the petitioner alone should be responsible for the operation of the Company, that during the mother's lifetime the income of the trust was to accumulate and to be added to principal, and that after her death the annual income was to be distributed equally among her three sons. (Ex. 2, R. 95, 96, 97, 102.)

The 1924 trust contained the admonition that it was the donor's earnest wish and request that unless there was, in Charles Bunting's judgment, some imperative necessity for the termination of said trust that he permit the same to continue in existence during his lifetime. (Ex. 2, R. 99.)

As time went on, Fannie Bunting realized that the 1924 trust was not altogether adequate to carry out the purposes she and her husband sought to accomplish,

namely, to insure the continuity of the Company's operations and the successful advancement of the Company's business. (R. 48.) In order to attain these ends, Fannie Bunting and the petitioner, on January 2, 1929, addressed a letter to The Toledo Trust Company, as Trustee, which terminated the 1924 trust and transferred the corpus thereof to Fannie Bunting. She thereupon transferred the property so withdrawn to The Toledo Trust Company, as Trustee, under a new trust indenture, dated January 2, 1929, designated in the files of The Toledo Trust Company as Trust No. 50. (Letter attached to Ex. 1, R. 92, 93; Ex. 1, R. 50-69.) It is the construction of this trust that is involved in these proceedings.

In Article V of Trust No. 50, Fannie Bunting declared that the primary purpose of creating said trust, the corpus of which consisted principally of Bunting Company shares, was to provide for the continuity and successful promotion and management of the Company after the death of her son, Charles, the petitioner herein, and that she "believes that by so doing she will most benefit the members of her family, who, if they retain their present interests in the Company, will be the ultimate beneficiaries of the trust." (Ex. 1, R. 58, 59.)

To accomplish this express purpose she provided that upon the termination of the trust, fifteen years after petitioner's death, the Bunting Company shares then in the trust were to be distributed among the then shareholders of The Bunting Brass & Bronze Company (Ex. 1, R. 64), exclusive of The Toledo Trust Company, as Trustee, under a certain trust established by the petitioner on January 2, 1929. (Ex. A to Ex. 1, R. 71-92.)

While the petitioner is given the power, during his lifetime, to modify, amend or add to the terms of the trust indenture, including the right to change the beneficiaries thereunder, or to revoke the same (R. 51), he never exer-

cised such power, except that by amendment in 1940 and again in 1941, he changed the persons who would be the ultimate beneficiaries of the corpus of the trust after his death. (Ex. 4, R. 105-110; Ex. 5, R. 110-115.)

Fannie Bunting in creating Trust No. 50, on January 2, 1929, was not actuated by the motive to circumvent income taxes or surtaxes, since, at that time, the income and surtax rates were very low.

At no time from the creation of Trust No. 50, not even during the depression years of the early '30s, has any distribution of income or principal been made to the petitioner from said trust and no distribution of any kind has ever been made therefrom to any other person. (R. 44, 48.)

The Trustee has accumulated the income annually received during the taxable years involved in the proceedings, namely: the years 1937 to 1941, inclusive, filed fiduciary income tax returns reporting such income and paid the income taxes due thereon. (Ex. 3, R. 104.)

By virtue of the rights vested in the petitioner under the terms of Trust No. 50, the respondent has determined that the petitioner is taxable for the whole of the income of Trust No. 50 during the tax years here involved.

Specification of Errors Now Urged.

The Circuit Court of Appeals erred:

1. In holding that the whole of the income of Trust No. 50, for the taxable years 1937 to 1941, inclusive, is taxable to the petitioner.

2. In holding that the underlying motive of petitioner's mother in creating Trust No. 50, namely, to preserve the continued successful management of The Bunting Brass & Bron[illegible]pany was immaterial.

Reasons for Granting the Writ.

Rule 38, Section 5, of the rules of this Court, specifies classes of cases in which applications for writs of *certiorari* to the Circuit Court of Appeals will be considered, to-wit:

> "Where a circuit court of appeals * * * has decided an important question of federal law which has not been, but should be settled by this court; or has decided a federal question in a way probably in conflict with the applicable decisions of this court; * * *."

It is submitted that in the present case:

1. The court below, in deciding that the mere donee of a power to alter, amend or revoke a trust, who is neither trustee nor beneficiary, is taxable upon the undistributed income of such trust because of the existence of such power, has decided an important question of federal law which has not been, but should be, settled by this Court.

2. The decision of the Appellate Court below probably conflicts with the decisions of this Court in the following cases: *Harrison vs. Schaffner*, 312 U. S. 579, and *Helvering vs. Horst*, 311 U. S. 112, and with the principles set forth by this Court in *Helvering vs. Grinnell*, 294 U. S. 153, and *Commissioner of Internal Revenue vs. Smith*, 324 U. S. 177, rehearing denied 224 U. S. 695.

Brief in Support of Petition for Certiorari

1. The Circuit Court of Appeals Decided an Important Question of Federal Law Which Has Not Been Settled by This Court.

The Circuit Court of Appeals affirmed the decision of the Tax Court of the United States. The Tax Court held that the powers granted to the petitioner by the trust instrument creating Trust No. 50 constituted the equivalent

of ownership of trust income for purposes of taxation. The Circuit Court of Appeals has, by concurring in the Tax Court's opinion, implicitly decided that the mere possession of the power to alter, amend or revoke the trust makes the income of the trust taxable to the donee of the power, even though the donee is neither grantor nor trustee nor beneficiary of the trust and does not now own, has never owned and may never own, the property from which the income derives.

This Court has not decided that question.

The Circuit Court of Appeals relied upon *Corliss vs. Bowers*, 281 U. S. 376. In that case, the grantor of a revocable trust, the income of which was payable to his wife for life, reserved the power to modify, alter or revoke the trust. The income of the trust was taxed to the grantor under the provisions of the Revenue Act of 1924 which are comparable to Sections 166 and 167 of the present Internal Revenue Code. This Court held that under those sections of the Revenue Act of 1924, the reservation by the grantor of a power to alter, amend or revoke made the income of the trust taxable to the grantor.

We concede that if Fannie Bunting, the creator of the trust, had reserved to herself the power to alter, amend or revoke the trust, the income thereof would, under the provisions of Sections 166 and 167 of the applicable revenue acts, been taxable to her, under the authority of the *Corliss* case, *supra*.

This Court did not, however, decide in the *Corliss* case, *supra*, nor has Congress by statute provided, that the undistributed income of a trust is taxable to the mere donee of a power to alter, amend or revoke.

On the contrary, Congress has created a distinction between the income of individuals and the income of property held in trust and has made a trust a separate taxable entity. Income accumulated for future distribution to

unascertained persons is not currently distributable within the meaning of Sections 161 and 162 of the applicable revenue acts and is taxable to the trustee. In *Corliss vs. Bowers, supra,* the income of the trust was not accumulated for future distribution to unascertained persons, but was paid to the taxpayer's wife. In that case, this Court applied the plain language of the applicable statute. In the instant case, inasmuch as the income has, under the specific terms of the trust, been accumulated for future distribution to unascertained persons, the income is under the plain and unequivocal language of Sections 161 and 162 of the applicable revenue acts taxable to the trustee.

The Circuit Court of Appeals also cited with approval *Emery vs. Commissioner,* 156 F. (2d) 728 (C. C. A. 1), cert. den. 329 U. S. 772; *Jergens vs. Commissioner,* 136 F. (2d) 497 (C. C. A. 5), cert. den. 320 U. S. 784; and *Richardson vs. Commissioner,* 121 F. (2d) 1 (C. C. A. 2). In each of these cases the reviewing court relied upon *Helvering vs. Clifford,* 309 U. S. 331. The principles enunciated in the *Clifford* case were not decisive of the questions presented in those cases and are even less decisive of the question here presented.

In *Helvering vs. Clifford, supra,* the settlor declared himself trustee of certain securities which he owned, the income from which, or such part thereof, as he in his discretion should determine, was to be paid to his wife. During the taxable year involved in the litigation, the entire income of the trust was paid to the wife. The trust was for a term of five years, subject to earlier termination upon the death of either the husband or the wife. Upon the termination of the trust, the corpus was to be distributed to the husband and all accrued, undistributed income to the wife. The husband retained full power to vote the securities, sell or exchange them, invest without restriction, collect the income and compromise all claims arising in the administration of the trust.

This Court held that the question presented was whether the husband was still the owner of the corpus. The short duration of the trust, the fact of the grantor's retention of control, the fact that the trust was created for the benefit of a member of the grantor's immediate family, and the fact that at the end of five years, the corpus reverted to the grantor, led the majority of the court to the conclusion that the husband remained the real owner of the trust *res* and that the entire income of the trust was, under Section 22(a), taxable to him.

It is apparent that the decision in the *Clifford* case is not applicable to the instant case, and in no way serves as authority for the holding of the Circuit Court of Appeals of the Sixth Circuit that the mere possession of a power to alter, amend or revoke a trust constitutes the realization of economic benefit, with the attendant result that the income of the trust is taxable to the donee of the power. Here, the petitioner is not the grantor of the trust. The trust is not a short-term family trust; at its termination, after the death of the petitioner, neither the income nor the principal of the trust is payable to petitioner's estate; Trust No. 50 is not a "temporary reallocation of income within an intimate family group" as the trust in the *Clifford* case was described.

In the *Emery* case, *supra*, which appears to be basis of the decision of the Circuit Court of Appeals in the instant case, the taxpayer's husband created five irrevocable trusts divesting himself of all interest in the trust corpus and income and naming a trust company as sole trustee.

Each trust was for the ultimate benefit of one of the Emerys' five children, subject to an annuity of $300 per month to be paid to the taxpayer, donor's wife.

The remainder of the income of the five trusts, which was in excess of $18,000, was to be distributed to such charities as Mrs. Emery might designate.

The taxpayer, Mrs. Emery, was vested with full power to revoke the trusts at any time and with the power to alter or amend. In the event of revocation, the corpus was to be distributed as she might determine.

In each of the taxable years before the court, 1939, 1940 and 1941, the trustee reported the annuity of $18,000 payable to Mrs. Emery as taxable to it on the ground that it was paid in satisfaction of an annuity. In 1939, the trustee reported the income in excess of the annuity, in the amount of approximately $11,000, as income set aside for charitable purposes.

In 1940, Mrs. Emery received, in addition to the annuity of $18,000, $7,800 from the trusts, which she reported as income to her, and, in 1941, she received, in addition to the annuity of $18,000 some $26,000, which she reported as income to her.

Upon these facts, the court found that the entire income of the trusts was taxable to Mrs. Emery.

The trusts considered by the court in the *Emery* case were family trusts established for the benefit of the immediate family of the donor. In the instant case, Trust No. 50 was established by Fannie Bunting for the purpose of insuring the continuing good management of the Company, founded and expanded by her husband. In the *Emery* case, the taxpayer, Mrs. Emery, received direct financial benefits from the trusts in the form of annuities, and, in addition thereto, in two of the taxable years before the court, received a portion of the income of the trusts in excess of the annuities. It cannot be controverted that Mrs. Emery received direct economic benefit from the five trusts established by her husband. In the instant case, Charles E. Bunting, the petitioner, has never received any income from the trust, nor directed its payment to another. Unlike Mrs. Emery, he has realized no economic benefit from the trust.

In the *Richardson* case, *supra*, the whole purpose of the trust, as the court concluded, was to defeat income taxes and surtaxes. The trust *res* had been Richardson's property, and under the terms of the trust created by his wife, to whom Richardson had given the property, the income of the trust was to be applied to the maintenance, education and support of Richardson's minor children, which relieved him of an obligation imposed upon him by law. He retained substantially all of the indicia of ownership which he had enjoyed prior to the creation of the trusts.

In the *Jergens* case, the husband, who had been the owner of the property, was given the power by his wife, the creator of the trust, to withdraw any or all of the corpus of the trust estate from the operation of the trust, and to amend, modify or revoke the trust. There was, as the court suggested, in reality no trust. Jergens retained substantially all the rights of ownership which he had enjoyed prior to the time he made the gift to his wife.

In each of these two latter cases, the trusts were devices to defeat the imposition of income taxes and surtaxes.

The question here presented is one which in the normal course of human relationship will frequently arise. It is only natural that the grantor of an *inter vivos* trust, or a testator who, by will, creates a testamentary trust, desires to vest discretion to alter or amend the terms of such trust in a person in whom he has confidence and thereby protect the trust estate against unforeseen contingencies. Whether or not the income from such a trust is taxable to the possessor of such powers is a matter of great importance not only to the person thus vested with the power, but also to the grantor or testator.

Trust No. 50, which was merely an enlargement of the trust plan adopted by Fannie Bunting in 1916 when she granted to the petitioner the voting rights in the Bunting

shares which she then owned, was clearly not a device for the avoidance of surtaxes as we have heretofore pointed out. It is doubtful whether Fannie Bunting would have created Trust No. 50 in its present form if she had believed that by so doing she would subject her son to tax upon income which he never received. Other grantors and testators may want to modify provisions of flexibility for future distribution, which they have incorporated in trusts and wills, if they know that such provisions will impose a financial hardship upon the donee of the power to make changes to meet unforeseen contingencies.

It is submitted that this Court has never decided that the income of a trust is taxable to the mere donee of a power to alter, amend or revoke the trust. That question is one of general interest which should be settled by this Court.

2. The Decision of the Appellate Court Below Probably Conflicts With the Applicable Decisions of This Court.

The decision of the Appellate Court below conflicts with the decisions of this Court in the following cases: *Helvering vs. Horst,* 311 U. S. 112, and *Harrison vs. Schaffner,* 312 U. S. 579, and with the principles set forth by this Court in *Helvering vs. Grinnell,* 294 U. S. 153, and *Commissioner of Internal Revenue vs. Smith,* 324 U. S. 177, rehearing denied 324 U. S. 695.

In all of the decisions of this Court from *Eisner vs. Macomber,* 252 U. S. 189, to the present time, this Court has held that a mere right to receive income does not, in and of itself, constitute income. Some realization of income must occur in order that taxation may follow. This realization need not be the receipt of cash or property, but may be the fruition of an economic gain or benefit to the taxpayer. However, without the element of economic bene-

fit, no income is realized or "derived" within the meaning of Section 22(a) of the Internal Revenue Code.

In *Helvering vs. Horst, supra,* the owner of certain bonds, in each of two years, delivered to his adult son "shortly before their due date," coupons clipped from the bonds owned by him. At maturity, later in the year in which the gift was made, the donee cashed the coupons. This Court upheld the Commissioner's ruling that the interest payments were taxable to the donor. This Court's decision was based upon the realization of economic benefit by the donor. The donor had received economic benefit by making gifts of income to his son. He had thus fully enjoyed the benefit of the economic gain which had inured to him when he acquired the right to receive the income. Having enjoyed the benefit, he could not escape taxation.

At page 115 of the opinion, this Court expressed the concept of realization in these words:

> "From the beginning the revenue laws have been interpreted as defining 'realization' of income as the taxable event * * *. And *'realization' is not deemed to occur until the income is paid.''* (Italics ours.)

and, at page 118:

> "The power to dispose of income is the equivalent of ownership of it. The *exercise* of that power to procure the payment of income to another is the enjoyment and hence the realization of the income by him who exercises it." (Italics ours.)

The petitioner herein has never procured nor attempted to procure the payment of income to himself or to any other person. No income or corpus has ever been withdrawn from the operation of the trust since its creation in 1929. The petitioner has never realized any economic benefit.

In *Harrison vs. Schaffner, supra,* the life beneficiary of a testamentary trust assigned specified amounts in dollars from the income of the trust to certain of her children for the year following the date of the assignment. By so doing, she exercised her control over the income of the trust and realized economic benefit. This Court decided that there was no distinction between a gift of income made prior to its receipt and a similar gift made after the receipt of income. In that case, this Court reviewed previous decisions relating to the realization of economic benefit and said at page 580:

> "Decision in these cases was rested on the principle that the power to dispose of income is the equivalent of ownership of it and that the *exercise of the power* to procure its payment to another, whether to pay a debt or to make a gift, *is within the reach of the statute taxing income 'derived from any source whatever'.*" (Italics ours.)

and, at page 582:

> "* * * It was for that reason that in each of those cases it was held that one vested with the right to receive income did not escape the tax by any kind of anticipatory arrangement, however skillfully devised, by which he procures payment of it to another, *since, by the exercise of his power to command the income,* he enjoys the benefit of the income on which the tax is laid." (Italics ours.)

The decision of the Circuit Court of Appeals in the instant case conflicts with the rule set forth in *Harrison vs. Schaffner, supra,* since Charles E. Bunting, the petitioner, has never exercised any power of command over the income of Trust No. 50.

Helvering vs. Grinnell, supra, is an estate tax case, but the principles there enunciated by this Court are applicable here.

In that case, a decedent had bequeathed a life estate to his widow with a general power of appointment. Provision was made for the distribution of the property in the event the widow failed to exercise such power. The widow by her will appointed the property to the same group who would have received it had she failed to exercise her power. After the death of the widow, the donees of the property renounced their right to receive the property under the will of the widow and elected to take under the will of the original decedent. This Court decided that the property passed under the will of the original decedent and that there was no effective exercise of the power of appointment. In that case, this Court decided that it was not the mere existence of a right which imposed tax liability, but, the effective exercise of such right.

In income taxation, the fundamental inquiry must always be whether the taxpayer realized income. The questions whether income is realized and when income is realized are frequently interdependent. In *Commissioner vs. Smith, supra,* these two questions coincided.

In that case, the taxpayer in 1934 received, as compensation from his employer, an option to purchase certain shares at a specified price, subject to certain contingencies. It was admitted that, in 1934 when he received the option, the value of the shares was less than the option price. In 1938, when the value of the shares had increased above the option price, the taxpayer exercised his option, and in 1939, when the value of the shares was still higher, he received delivery of the shares. This Court held that the taxpayer had received income in 1939 in an amount equal to the difference between the option price and the fair market value of the shares in that year. The Court's decision was based upon Section 22(a) of the Revenue Act of 1938. Implicit in the Court's decision is the holding that the taxpayer received compensation only when there was a realization

of economic benefit. The option itself, given in 1934, did not result in income, since the optionee would never have received any additional compensation, if the option had never been exercised.

Upon rehearing, this Court said, at page 696:

> "The Tax Court found that respondent received compensation 'when (he) exercised his option and received the stock' * * *. This conclusion of the Tax Court finds ample support in the record, and we concur in it."

Assuming the market value of the shares exceeded the option price in 1937, Smith, by exercising his option and receiving the shares in that year, would have realized income and been subject to tax. He did not do so and by depriving himself of income deprived the Treasury of tax. If, in any given year in which Trust No. 50 enjoyed income, Charles E. Bunting, the petitioner, had exercised his right to command the income, he obviously would have realized income and been subject to tax. He has not done so but has deprived himself of the income and of any and all economic benefit from the trust in each year since the date of its creation in 1929.

The decision of the Circuit Court of Appeals conflicts with the principles expressed, and the concept of income established, by this Court in *Commissioner of Internal Revenue vs. Smith, supra.*

Conclusion.

The decision of the court below presents an important question of federal law which has not been, but should be, settled by this Court. This Court has never decided that the donee of a power to alter, amend or revoke a trust, who is neither the beneficiary nor trustee thereof and who has never exercised or attempted to exercise such power, is to

be taxed upon the income of the trust which has been accumulated for future distribution. Further, the decision of the court below—that the undistributed income of the trust established by the petitioner's mother is taxable to the petitioner, who has never realized economic benefit from the trust—probably conflicts with the applicable decisions of this Court.

For these reasons we submit that this petition for a writ of *certiorari* to the United States Circuit Court of Appeals for the Sixth Circuit should be granted.

Respectfully submitted,

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APPENDIX

The pertinent provisions of the Revenue Acts of 1936 and 1938 are as follows:

"SEC. 22. GROSS INCOME.

"(a) General Definition—'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, business, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *"

"SEC. 161. IMPOSITION OF TAX.

(a) Application of Tax—The taxes imposed by this chapter upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

(4) Income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) Computation and Payment—The Tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary, except as provided in section 166 (relating to revocable trusts) and section 167 (relating to income for the benefit of the grantor)."

"SEC. 162. NET INCOME.

" • • •

"(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the legatees, heirs, or beneficiaries, but the amount so allowed as a deduction shall be included in computing the net income of the legatees, heirs, or beneficiaries whether distributed to them or not. As used in this subsection, 'income which is to be distributed currently' includes income for the taxable year of the estate or trust which, within the taxable year, becomes payable to the legatee, heirs, or beneficiary. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year;"

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In the Supreme Court of the United States

OCTOBER TERM, 1947

No. 588

CHARLES E. BUNTING, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 27–40) is not reported. The opinion of the Circuit Court of Appeals (R. 127–134) is reported in 164 F. 2d 443.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered November 24, 1947. (R. 126.) The petition for a writ of certiorari was filed February 12, 1948. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Taxpayer's mother created a trust which vested in him complete command over the trust property and income, including the power to revoke the trust at any time and appropriate all the trust funds. Did the court below err in affirming the Tax Court's decision that the trust income was includible in taxpayer's gross income as defined in Section 22 (a) of the Internal Revenue Code and the applicable Revenue Acts?

STATUTES INVOLVED

These appear in the Appendix, *infra,* pp. 12–15.

STATEMENT

The facts found by the Tax Court (R. 28–39) may be summarized as follows:

Taxpayer and his mother in 1924 owned a majority of the shares of stock of Bunting Brass and Bronze Company, the remaining shares being owned by taxpayer's two brothers. On January 18, 1924, taxpayer's mother, for the primary purpose of insuring management of the corporation by taxpayer, transferred her shares in trust to the Toledo Trust Company. Article IV of the trust instrument directed the trustee to dispose of all or any portion of the trust property in accordance with "any written directions" of taxpayer, authorized taxpayer to "withdraw all or any part of said Trust Property by written directions to Trustee", and absolved the trustee of liability

"for anything done in accordance with instructions" of taxpayer. This article further provided that should taxpayer "withdraw all of the Trust Property, this Trust shall thereafter be considered as terminated" unless taxpayer otherwise directed (R. 28–30.)

In order more completely to accomplish the purposes of this trust, taxpayer and his mother decided in 1929 to terminate it and create a new one. (R. 31.) Accordingly, exercising the authority vested in him by Article IV of the 1924 trust instrument, taxpayer on January 2, 1929, addressed a letter to the trustee, signed by himself and his mother, notifying the trustee that he was withdrawing all of the trust property and simultaneously transferring it to his mother, who in turn was simultaneously retransferring the property to the trustee. At the same time, taxpayer's mother executed a new trust instrument conveying to the trustee all of the property theretofore held in the 1924 trust. (R. 31–32.) This second trust is the one whose income is here involved. At the time of its creation in 1929 the trust estate consisted of 2,385 shares of common stock of the Bunting Brass and Bronze Company, about $70,000 worth of miscellaneous securities, and about $4,820 in cash. (R. 38.)

Article II of the 1929 trust instrument provided as follows (R. 32–33):

> Powers of Donor's Son, Charles E. Bunting.

Notwithstanding any other provision herein contained the Donor's son, Charles E. Bunting, may at any time or from time to time during his lifetime (either before or after the death of the Donor), without the consent or approval or joinder of the Donor or of any beneficiary hereof or the consent or approval of any court or other authority, by the delivery of a written order to the Trustee, (a) modify, amend or add to this agreement in any respect whatsoever, including the right to change the beneficiaries hereunder, their shares and the plan of distribution to each and to appoint himself as beneficiary hereof, provided, however, that the duties, powers and liabilities of the Trustee shall not be substantially changed without its prior written consent, (b) withdraw any of the trust property from the operation of this agreement whereupon such property shall be paid and delivered over to the Donor's said son, or (c) revoke this agreement in its entirety, whereupon the entire property then held in trust shall be paid and delivered over to the Donor's said son and this trust shall thereupon terminate; and the Donor's said son shall be under no duty or obligation to account to the Donor or the Trustee or any beneficiary hereunder or to any court or other authority for the application of the trust property so received by him upon the exercise of such power of withdrawal or revocation or by

appointment as such beneficiary, but the same shall be his absolutely.

Article III granted various powers to the trustee, all of which were made "Subject to the control and written directions" of taxpayer. (R. 33–35.) Article IV provided that "In the absence of any direction to the contrary" by taxpayer and "subject in all respects to the exercise of all other powers" conferred upon taxpayer, the net income of the trust was to be accumulated during the joint lives of taxpayer and his mother; that after the mother's death the net income was to be "disposed of in accordance with the written directions" of taxpayer and subject to the exercise by taxpayer of all his other powers; and that after taxpayer's death both principal and accumulated income were to be held subject to the provisions of Article V. (R. 35, 36–37.) Article VII authorized taxpayer to remove the trustee at any time by written notice; in the event of resignation, removal or incapacity of the trustee, taxpayer was authorized to name the successor by a written instrument. (R. 36.)

Exercising some of the powers vested in him by Article II of the 1929 trust instrument, taxpayer on July 12, 1940, struck out the provisions of Article V (relating to distribution of the trust property after his death) and substituted a new one which changed the interests of the beneficiaries. On July 2, 1941, taxpayer again revised the provisions of Article V. (R. 38.)

Taxpayer's mother died in 1938. At no time did taxpayer receive any distribution of income or principal from either the 1924 or 1929 trust, and no distribution of any kind has been made to any person from either of the trusts. (R. 38.)

For the years 1937 through 1941, the taxable years, the trustee filed fiduciary income tax returns in which it reported and paid the tax on the net trust income. (R. 39.) The Commissioner ruled that the income was taxable to taxpayer under Sections 22 (a), 166 and 167 of the applicable Revenue Acts and the Internal Revenue Code, and determined deficiencies accordingly. (R. 14–24, 27.) The Tax Court held that by virtue of the powers vested in taxpayer under the 1929 trust instrument he was the owner of the trust income for purposes of Section 22 (a), and sustained the Commissioner; in view of that holding the Tax Court considered it unnecessary to decide whether taxpayer was alternatively taxable on the income under Sections 166 and 167. (R. 39–40.) The court below agreed with the Tax Court. (R. 127–134.)

ARGUMENT

1. The decision below is in accord with the settled rule that one who has power to revoke a trust and receive either the income or the income-producing principal is taxable on the trust income. It is immaterial that the possessor of the power is someone other than the settlor, and that he did not

exercise the power in his own favor. ***Emery*** v. ***Commissioner,*** 156 F. 2d 728 (C. C. A. 1st), certiorari denied, 329 U. S. 772; ***Mallinckrodt*** v. ***Nunan,*** 146 F. 2d 1 (C. C. A. 8th), certiorari denied, 324 U. S. 871, rehearing denied, 325 U. S. 892; ***Jergens*** v. ***Commissioner,*** 136 F. 2d 497 (C. C. A. 5th), certiorari denied, 320 U. S. 784; ***Richardson*** v. ***Commissioner,*** 121 F. 2d 1 (C. C. A. 2d), certiorari denied, 314 U. S. 684, rehearing denied, 314 U. S. 714; ***Commissioner*** v. ***Newman,*** 159 F. 2d 848 (C. C. A. 2d); see also ***Stix*** v. ***Commissioner,*** 152 F. 2d 562 (C. C. A. 2d); ***Busch*** v. ***Commissioner,*** 148 F. 2d 798 (C. C. A. 8th); ***Frank*** v. ***Commisioner,*** 145 F. 2d 413 (C. C. A. 3d); ***Richardson*** v. ***Commissioner,*** 151 F. 2d 102 (C. C. A. 2d), certiorari denied, 326 U. S. 796.[1] These decisions are rooted in the fundamental principle that taxation is less concerned with refinements of title than with command over property (***Corliss*** v. ***Bowers,*** 281 U. S. 376; ***Helvering*** v. ***Clifford,*** 309 U. S. 331), and the familiar corollary that the power to dispose of income is tanta-

[1] An addition to Treasury Regulations 111, promulgated under the Internal Revenue Code, made by T. D. 5488, 1946-1 Cum. Bull. 19, and consisting of Section 29.22 (a)-22 of the Regulations, expresses the law reflected in these and similar decisions by providing that—

"Where a person other than the grantor of property transferred in trust has a power exercisable solely by himself to vest the corpus or the income therefrom in himself, the income therefrom shall be included in computing the net income of such person. * * *"

mount to ownership of it for tax purposes (*Helvering* v. *Horst,* 311 U. S. 112; *Harrison* v. *Schaffner,* 312 U. S. 579).

The contentions made by taxpayer in the petition for certiorari are essentially the same as those advanced in the petitions for certiorari in the *Emery, Mallinckrodt, Jergens,* and *Richardson* cases, *supra.* Nothing has occurred since the denial of certiorari in those cases which calls for further review of this case.

By virtue of the powers vested in him by Article II of the trust instrument (R. 32–33), taxpayer enjoyed throughout his lifetime complete and unqualified control over both the principal and income of the trust. Indeed, a more absolute command over property and its income could hardly be imagined. At any time during the taxable years taxpayer could have completely rewritten the terms of the trust or modified it "in any respect whatsoever." He could have directed that the entire income be paid to himself, to his creditors, or to any other person; or he could have directed withdrawal and payment to himself of any portion of the principal, including accumulated income; or he could have completely revoked the trust and appropriated the entire trust fund to himself. To exercise any of these choices taxpayer had only to make "delivery of a written order to the Trustee," and he could do so "without the consent or approval or joinder of the

Donor or of any beneficiary hereof or the consent or approval of any court or other authority." He was "under no duty or obligation to account" to any one for application of any of the trust funds he chose to withdraw for himself; they were to be "his absolutely." All that taxpayer lacked was bare legal title, and even this he could secure at will by simply addressing a letter of revocation to the trustee. In the light of the controlling decisions the Tax Court's conclusion (R. 39) that the powers vested in taxpayer "constitute the equivalent of ownership of the trust income for purposes of taxation" is unassailable. As the court below stated (R. 133) in agreeing with the Tax Court, taxpayer had "unfettered command" of the trust income. Certainly the command enjoyed by taxpayer here was no less comprehensive than that possessed by tht taxpayers in the *Emery, Mallinckrodt, Jergens* and *Richardson* cases, *supra.*

2. *Helvering* v. *Horst, supra,* and *Harrison* v. *Schaffner, supra,* relied upon by taxpayer for conflict (Br. 15–17), confirm rather than impugn the correctness of the decision below. The statement of this Court (*Horst,* p. 118; *Schaffner,* p. 580), that "The power to dispose of income is the equivalent of ownership of it" applies with full force here. In those cases the "exercise" of the power to dispose of the income consisted of an affirmative act of assignment by the taxpayer to

others, whereas here (as in the *Emery, Mallinckrodt, Jergens* and *Richardson* cases, *supra*), it consisted of the taxpayer's failure to demand the income for himself; but whether the power of disposition is affirmatively or negatively exercised is of no significance. In support of its decisions in the *Horst* and *Schaffner* cases this Court cited *Corliss* v. *Bowers, supra,* wherein it had stated (p. 378) that the income which one "is free to enjoy at his own option may be taxed to him as his income, whether he sees fit to enjoy it or not", and that "it does not matter whether the permission [that another enjoy the income] is given by assent or by failure to express dissent". See also *Emery* v. *Commissioner, supra,* p. 730.[2]

The case of *Helvering* v. *Grinnell,* 294 U. S. 153, relied upon by taxpayer (Br. 15, 17–18), is irrelevant. It involved an estate tax statute which, in its then form, required that property "pass" under the exercise of a general power of appointment to be includible in the estate of the donee of the power.

Commissioner v. *Smith,* 324 U. S. 177, rehearing denied, 324 U. S. 695, also cited by taxpayer

[2] In asserting conflict with the *Horst* and *Schaffner* cases (Br. 15–17) taxpayer apparently confuses the question of *who* is taxable on the income with *when* it is taxable. The trust here involved was taxable to taxpayer because of his unqualified right to demand it (or the income-producing corpus) from the trustee; the income was "realized," and hence taxable, in the respective taxable years it was earned by the trust corpus.

(Br. 15, 18–19), is likewise inapposite. There an employee received compensation in the form of an option to purchase stock at a price higher than its then market value, and exercised the option after the value of the shares had risen above the option price; the question was whether the compensation includible in the employee's gross income was to be measured by the valueless option or included the amount obtained upon later exercise of the option. That question is far removed from the one here presented.

CONCLUSION

The decision below is correct. There is no conflict, and no occasion for further review. The petition should therefore be denied.

Respectfully submitted.

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MARCH 1948.

APPENDIX

Internal Revenue Code:

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

(26 U. S. C. 1940 ed., Sec. 22.)

SEC. 161. IMPOSITION OF TAX.

(a) *Application of tax.*—The taxes imposed by this chapter upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

(4) Income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) *Computation and payment.*—The tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary, except as provided in section 166 (relating to revocable trusts) and section 167 (relating to income for benefit of the grantor).

* * * * *

(26 U. S. C. 1940 ed., Sec. 161.)

SEC. 162. NET INCOME.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

* * * * *

(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year;

(c) in the case of income received by estates of deceased persons during the

period of administration or settlement of the estate, and in the case of income which, in the discretion of the fiduciary, may be either distributed to the beneficiary or accumulated, there shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year, which is properly paid or credited during such year to any legatee, heir, or beneficiary, but the amount so allowed as a deduction shall be included in computing the net income of the legatee, heir, or beneficiary. (26 U. S. C. 1940 ed., Sec. 162.)

SEC. 166. REVOCABLE TRUSTS.

Where at any time the power to revest in the grantor title to any part of the corpus of the trust is vested—

(1) in the grantor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom, or

(2) in any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom,

then the income of such part of the trust shall be included in computing the net income of the grantor. (26 U. S. C. 1940 ed., Sec. 166.)

SEC. 167. INCOME FOR BENEFIT OF GRANTOR.

(a) Where any part of the income of a trust—

(1) is, or in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition

of such part of the income may be, held or accumulated for future distribution to the grantor; or

(2) may, in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition of such part of the income, be distributed to the grantor; or

* * * * *

then such part of the income of the trust shall be included in computing the net income of the grantor. (26 U. S. C. 1940 ed., Sec. 167.)

Sections 22 (a), 161, 162, 166 and 167 of the Revenue Act of 1936, c. 690, 49 Stat. 1648, and of the Revenue Act of 1938, c. 289, 52 Stat. 447, are identical.

U. S. GOVERNMENT PRINTING OFFICE: 1948